

E U R O P E A N E C O N O M I C A R E A
S T A N D I N G C O M M I T T E E
O F T H E E F T A S T A T E S

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SUBCOMMITTEE II ON FREE MOVEMENT OF CAPITAL AND SERVICES

**EFTA COMMENTS ON THE GREEN PAPER
“TOWARDS FAIR AND EFFICIENT PRICING IN TRANSPORT”**

1. The EFTA States consider the Green Paper on “Fair and Efficient Pricing” as an important contribution to the international discussion on internalising external costs of transport. Furthermore, the EFTA States are of the opinion that the Green Paper could provide a basis for developing internalisation as an efficient instrument in European transport policy.

External costs and internalisation in the EFTA States

2. The EFTA States would like to point out that considerable geographical variations can be observed and thus to emphasise the need for differentiated implementation of internalisation at national and local level. Some EFTA States bear, at least on part of their national territory, the same considerable external costs stemming from road traffic in general and road transit in sensitive areas (alpine regions) in particular (congestion, pollution) as most European Union Member States of central Europe. In other EFTA States, i.e. the whole territory of Iceland and most rural areas in Norway, costs stemming from congestion, local air pollution and noise are minor or negligible.

3. The EFTA States have already made some efforts in order to establish tax schemes that allow for internalisation of external costs. Iceland and Norway have gathered some experience with the kilometre tax and annual vehicle taxes exist in all EFTA States. The Norwegian tax system also comprises environmental taxes on carbon, lead and sulphur in petrol and autodiesel. The lead and sulphur taxes are differentiated according to the content of these substances in different fuels. To reduce local congestion and pollution problems during peak hours, the Norwegian Government has formally allowed and encouraged the use of time differentiated taxes in the toll rings around the three largest Norwegian cities (established for the purpose of financing infrastructure investments). Such time differentiation is expected to have a considerable potential for reducing external costs during peak hours. Local authorities have to little extent implemented this instrument, and present use of time differentiation is considered to have marginal influence on the distribution of traffic over time.

The concept of internalisation

4. Establishing some kind of international regulatory framework for efficient pricing in transport may be necessary and helpful for concrete new policy actions at national or local level. It is, however, essential that any future work on these issues that may be undertaken by the European Union is closely coordinated with or preferably integrated into other relevant activities, e.g. the ECMT Task Force on social costs of transport.

5. The Green Paper clearly calls for further work and clarification on unsolved methodological and implementation problems. The EFTA States would especially like to mention the need for:

- a precise and commonly accepted definition of external costs and possible external benefits, among other things it will be necessary to clarify which parts of the capital costs of the infrastructure should be treated as marginal, external and to standardise methods to calculate traffic dependent maintenance costs;
- refined valuation methods;
- the development and the standardisation of necessary cost-effective reliable technologies at acceptable costs and which fulfil the requirements of interoperability and compatibility.

International regulatory framework

6. It must be emphasised that taxes in the EFTA States are decided by national and local authorities without any restrictions due to EU regulations in this field. Furthermore, introduction of charges to reflect external costs of transport should be decided at national or local level to reflect necessary differentiation. It clearly appears, however, that among other factors, increased liberalisation of transport markets means that international regulations may be a prerequisite for internalisation to avoid unintended distortions of competition between transport modes or operators from different countries. Road user charges may also require an international system for reallocation of revenue between states.

Efficient pricing - internalisation of external costs

7. The EFTA States strongly support that marginal, external costs of transport should be internalised through taxes, for which national or local competence is exclusive. To stimulate efficient resource allocation in the transport system all modes of transport should be taxed according to their marginal, external costs. At present, air and sea transport are exempted from different taxes, e.g. environmental taxes. To allow efficient pricing across different transport modes it is important to facilitate the use of environmental taxes also in air and sea transport. Furthermore, the Green Paper focuses the external costs of heavy goods vehicles, especially in its proposals for short term policy actions. The EFTA States would like to underline that passenger cars represent the major part of traffic flows and that increased passenger transport by car consequently

is the main reason for the present level of external costs. The EFTA States will underline that proposals on new taxes in order to internalise different kinds of external costs must take into consideration to which extent existing taxes levied on each transport mode already reflect its marginal, external costs.

8. The EFTA States are also convinced that internalisation of external costs of transport should be regarded as part of a comprehensive transport policy as pointed out in paragraph 3 of the executive summary in the Green Paper. The potential benefits from increased rail and sea transport seem quite clear. A realistic assessment of present capacity and quality of these modes, however, indicates rather limited possibilities for transferring goods from road transport in the short and medium term. This means that a policy for more efficient pricing in transport must be integrated in a comprehensive strategy which contains other measures aimed at strengthening the competitive position of rail and sea transport.

9. The EFTA States believe that internalisation of external costs will not only stimulate more efficient transport, but also improve the efficiency of the economy as a whole and induce less environmentally damaging patterns of transport behaviour. The revenues raised from new taxes intended to reflect external costs will make reductions in other taxes (e.g. on labour) possible. Thus green taxes may achieve both environmental improvements and gains in economic efficiency.

10. It must be stressed that internalisation probably must be implemented by designing packages of different taxes/charges. External costs which differ relatively little across place and time, e.g. infrastructure damage and global/regional pollution, could be internalised through national taxes, such as fuel, vehicle or kilometre taxes. On the other hand local pollution and congestion problems, mostly located in city regions and other densely populated areas, are most effectively reflected through differentiated road pricing.

11. The EFTA States agree that transport taxes must be differentiated to reflect variations in costs depending on time, place and mode/vehicle. They also share the view that electronic road pricing in the long run probably will make rather sophisticated differentiation feasible. Nevertheless, it will be important to balance the benefits from almost perfect differentiation and increasing administrative costs. The possibility to implement detailed differentiation is crucial in systems for internalising costs related to congestion, local air pollution and noise in city regions.

12. The EFTA States perceive pricing according to marginal, external costs to be the cornerstone of the Green Paper. Nevertheless, the conclusions are somewhat unclear because the Green Paper also seems to advocate that transport tax revenues in principle should equal total infrastructure costs. The Green Paper addresses three different questions and to some extent deals with efficient pricing to secure efficient use of resources, equity considerations and optimal financing of public budgets as if they were one issue.

13. The EFTA States agree that the three questions are closely linked, but they are of the opinion that the Green Paper should have focused on efficient pricing without mixing it with equity and public finance. The two latter issues are not relevant in the context of the internal market and are furthermore of national competence. The debate should really focus on efficient pricing.

The principle of costs recovery

14. The Green Paper stresses that fair and efficient pricing means that all kinds of transport should cover their infrastructure costs. According to the Green Paper investments for non-transport related policy reasons are regarded as irrelevant in relation to the principle of costs recovery. Costs recovery seems to imply ear-marking of the revenue from transport taxes which is in conflict with principles for optimal financing of public deficits.

15. Internalising through taxes equivalent to marginal, external costs is essential to obtain efficient use of scarce resources as mentioned earlier. Furthermore, taxation of external costs represents the most efficient way to finance the public sector. It might be rational to impose additional charges on transport to raise revenue, but only if the costs (i.e. loss of efficiency in the economy) are regarded as lower than for other tax options. Public revenues should be spent according to expected benefits from alternative use without any restrictions regarding different sectors' contributions to the total revenue.

16. Although this may easily lead to inefficient allocation of resources, there are several examples of earmarking of tax revenues, also in the EFTA States. Such earmarking is usually implemented to increase the acceptability of new taxes and to obtain necessary political support. It would be a better solution to propose efficient pricing of transport through taxes at the same time as proposals for public expenditure on environmental/investment programmes financed from general budgets. This linkage in time could secure necessary political acceptance without inefficient earmarking. It is an important prerequisite that the suggested programmes be based on proper evaluations of socio-economic consequences.

Short term policy action

17. Being aware that there are some unsolved methodological questions and considerable uncertainty as to the actual size of different external costs, the Commission indicates possible short term steps towards internalisation. The EFTA States appreciate this attitude. Differentiation of fuel and vehicle taxes would be cost-effective instruments to reduce road damage and environmental problems. The EFTA States also consider positively the suggestion to consider the introduction of an electronic kilometre tax which probably will require an international regulatory framework.

18. A kilometre tax can be differentiated to reflect differences in external costs from road damage and global/regional pollution between vehicles. A fuel tax cannot reflect differences in specific emissions or the progressive growth in road damage with

increasing total weight of vehicles as good as a kilometre tax (even if it is combined with an annual vehicle tax). On the other hand fuel taxes may have some administrative advantages compared to the kilometre tax. The EFTA States have some experience regarding kilometre tax. Norway had a kilometre tax until 1993 and Iceland still has such a system. One of the problems concerning a kilometre tax is the possibility of tampering with the meters. Great emphasis must therefore be put on the development of tamperproof meters. A kilometre tax would be rather complicated to administer, and efforts to minimize compliance costs should be made.

Conclusion

19. The EFTA States are of the opinion that it is necessary to design Europe's transport policy by taking into account true costs of transport. The EFTA States therefore support the Commission and encourage the European Union to take further steps in order to facilitate efficient pricing. It must be emphasised that taxes are not included in the EEA Agreement and therefore remain of the sole competence of the EFTA States. However, to allow increased internalisation without unintended distortions of competition between transport modes or operators from different countries close cooperation between the European Union and other European States will be essential in future development of policy in this field.

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